Insights, Tacit Thought | Weekly Investment Insights

Lessons from this week

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The world was expecting the second presidential term of Donald Trump to take an unconventional and rough tackle approach to most issues, but what we have witnessed in little over the past week goes far beyond what even members of his own inner circle had envisaged. Equity and bond markets fell in tandem as the risk of a recession, coupled with higher prices (inflation), have led to the perfect storm for investors, governments and companies.

One point we feel the need to reiterate this week: sudden outsized movements in prices catch many large speculative traders on the wrong side of the movement and there is a risk that cracks may open in the complex, interconnected international financial markets. This is a structural issue driven by regulatory changes following the 2008 market crash and leads to significantly larger and quicker readjustments to prices when unexpected events occur.

As we do not hold speculative positions or leverage in our strategies, the Tacit approach to this type of market event is to not make any knee jerk reactions and, more importantly, to focus on what this means looking forward over the coming months and years as markets discount the known news very quickly but tend to overreact in both directions. With hindsight, it is always better to enter periods such as this with no exposure to investment assets, however this would have hurt last year when our strategies delivered healthy positive real returns.

In short, the key lessons from this week are not new to our readers but we feel it is important to restate them clearly:

1. Timing the markets is extremely difficult
2. An overreliance on one economy, the US in this cycle, is ultimately risky
3. Regional and bilateral trade will become more prevalent over global trade
4. Valuations do matter, as expensive assets are most susceptible when unexpected events occur, whilst cheaper assets provide a buffer to falls
5. Diversification does help, but cannot totally offset falls of the magnitude we experienced over the past week

What comes next?

More uncertainty day to day is inevitable and investors will be more cautious as this period will live long in the memory. Ultimately though, a line has been drawn under how far the US authorities are willing to go in their pursuit of the MAGA agenda.

Our primary focus now is on reassessing the assets we own in the Growth element of strategies for two reasons. Firstly, assessing any material changes in the underlying cashflows over the medium term which would alter the investment thesis for owning them. Secondly, and just as important after the market volatility, considering the current market pricing of the growth investments we own and adjusting the weightings to take advantage of the outsized moves we have seen. A secondary focus is to consider which other assets, such as European and Asian technology companies for example that trade at significantly discounted valuations to their US peers historically, may well provide an opportunity in the new environment as regional champions replace the global champions of today.

Within our Stabiliser component, the government bond exposures have actually risen over the past month, albeit that they have become more volatile over the past days. This is a reminder of the importance of these assets for our lower risk strategies as they do ultimately mitigate losses during periods such as this. Within this component, the actions of the US

authorities to undermine the role of the US$ as the preeminent global reserve currency has led us to reevaluate the role of other sovereign bonds such as German Bunds and Chinese government bonds as Stabilisers for UK investors moving forward.

We will be hosting our regular quarterly webinar later this month (register here) and would urge all readers to register to hear the Tacit team's views first hand

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